MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2016/2017

PPE0054 – BASIC MACROECONOMICS

(Foundation in Business)

22 OCTOBER 2016
2.30 p.m. – 4.30 p.m.
(2 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of **TWELVE** pages.
2. Answer **ALL** questions in **Section A** and **B**.
3. The answers for **Section A** should be shaded on the OMR sheet. The answers for **Section B** should be written in the Answer Booklet.

SECTION A: MULTIPLE CHOICE QUESTIONS [40 MARKS]

Instructions: Answer **ALL** questions in this section. Shade the answers on the **OMR** sheet.

1. When using the income approach to estimate Gross Domestic Product (GDP), which of the following would **NOT** be included?
   A. Proprietors' income
   B. Personal consumption expenditures
   C. Net interest received by households
   D. The rental value of owner-occupied housing

2. An example of an increase in gross investment spending that also increases Gross Domestic Product (GDP) is when_____.
   A. a farmer buys a used tractor
   B. a family sells its home because of a transfer
   C. government increases spending on infrastructure
   D. inventories of new cars accumulate on the lots of car dealers

3. The farmer pays 20 cents for the seed that is sold to the miller for 35 cents; the miller makes flour and sells it to the baker for 55 cents. The baker makes bread and sells it to the grocery store for 80 cents and the store sells it to consumers for RM1.00. The contribution to Gross Domestic Product (GDP) is_____.
   A. RM2.90
   B. RM1.90
   C. RM1.00
   D. 20 cents

Refer to ***Exhibit 1*** for question no.4. ***Exhibit 1*** shows data on nominal GDP and real GDP (values are in billions of dollars).

Year	Nominal GDP	Real GDP
2007	14,078	13,254
2008	14,441	13,312

Exhibit 1

4. Based on ***Exhibit 1***, GDP deflator for 2008 equals_____.
   A. 92.2
   B. 102.6
   C. 108.5
   D. 109.1

5. The output of U.S. citizens who work in Canada would be included in the_____.
   A. gross national product of Canada
   B. gross domestic product of Canada
   C. gross domestic product of the United States
   D. gross national product of Canada and the gross national product of the United States

Continued...

6. When the price level rises, the real interest rate _____ and the quantity of real GDP demanded _____.
   A. falls; increases
   B. rises; increases
   C. falls; decreases
   D. rises; decreases

7. If the marginal propensity to save is 0.25, then a RM10,000 decrease in disposable income will _____.
   A. increase consumption by RM7,500
   B. increase consumption by RM2,500
   C. decrease consumption by RM7,500
   D. decrease consumption by RM2,500

8. To eliminate an inflationary gap using fiscal policy, the government could _____.
   A. increase taxes
   B. decrease the quantity of money
   C. increase government expenditure on goods and services and simultaneously increase taxes by an equal amount
   D. increase government expenditure on goods and services and simultaneously decrease taxes by an equal amount

9. If the multiplier is 5, the slope of the aggregate expenditure (*AE*) curve is _____.
   A. 0.5
   B. 0.6
   C. 0.8
   D. 0.2

10. If disposable income falls by $50 billion and consumption falls by $40 billion, then the slope of the consumption function is _____.
   A. 1.20
   B. 0.80
   C. 0.70
   D. 0.10

11. If Joe withdraws a RM100 bill from his checking account and Jack deposits another RM100 bill in his savings account, by how will M1 and M2 change?
   A. M1 will increase, and M2 will increase.
   B. Both M1 and M2 will remain the same.
   C. M1 will decrease, but M2 will remain the same.
   D. M1 will remain the same, and M2 will increase.

12. The unit of account is defined as _____.
   A. the medium of exchange
   B. an object that is accepted in return for goods and services
   C. an agreed upon measure for stating prices of goods and services
   D. the exchange of goods and services directly for other goods and services

Continued...

13. Suppose that AZ Bank has excess reserves of RM20,000, required reserves of RM80,000 and the required reserve ratio is 5 percent. What are the total amounts of deposits in this bank?
    A. RM100,000
    B. RM180,000
    C. RM1,000,000
    D. RM1,600,000

14. If the required reserve ratio increases, then _____.
    A. banks are able to make more loans
    B. banks can buy more government securities
    C. bank customers become more willing to make deposits in banks
    D. banks' required reserves increase and their excess reserves decrease

15. Lowering the discount rate will _____.
    A. decrease reserves, encourage banks to make fewer loans, and decrease the money supply
    B. decrease reserves, encourage banks to make fewer loans, and increase the money supply
    C. increase reserves, encourage banks to make more loans, and increase the money supply
    D. increase reserves, encourage banks to make more loans, and decrease the money supply

16. If the central bank buys Treasury bills, this will shift the _____.
    A. money supply curve to the left
    B. money demand curve to the left
    C. money supply curve to the right
    D. money demand curve to the right

17. The quantity equation states that _____.
    A. $M - V = P - Y$.
    B. $M \times V = P \times Y$.
    C. $M + V = P + Y$.
    D. money supply (M) divided by the velocity of money (V) equals the price level (P) divided by real output (Y), i.e., $M/V = P/Y$.

18. A person puts a $100 bill in the glove compartment of his car in case of an emergency. This is an example of _____.
    A. the transaction demand for money
    B. the investment demand for money
    C. the speculative demand for money
    D. the precautionary demand for money

Continued...

19. Excess demand in the money market causes _____.
    A. a decrease in the money supply
    B. a decrease in the equilibrium interest rate
    C. an increase in the equilibrium interest rate
    D. an increase in the quantity demanded of money

20. The menu cost of inflation involves _____.
    A. higher food prices
    B. cost-of-living adjustments
    C. the costs associated with changing price lists
    D. the mistake people make when they do not know the actual rate of inflation

21. The inflation rate has been 4 percent for twenty years, and the nominal interest rate has been 8 percent during this same time period. Suddenly, the public anticipates that the inflation rate will be 8 percent this coming year. The real rate of interest for the coming year is _____.
    A. 0 percent
    B. 2 percent
    C. 4 percent
    D. 6 percent

Refer to ***Exhibit 2*** for question no.22. ***Exhibit 2*** shows the values of the consumer price index for 1996, 1997, and 1998.

Year	CPI
1996	157
1997	161
1998	163

Exhibit 2

22. Based on ***Exhibit 2***, the inflation rate for 1997 was equal to _____.
    A. 1.2 percent
    B. 2.0 percent
    C. 2.5 percent
    D. 4.0 percent

23. Demand pull inflation can be started by _____.
    A. a decrease in net exports
    B. an increase in the price of oil
    C. a decrease in the quantity of money
    D. an increase in government spending

24. If you have trouble finding a job because of a slowdown in the overall economy, we would say that you are _____.
    A. cyclically unemployed
    B. seasonally unemployed
    C. frictionally unemployed
    D. structurally unemployed

Continued...

25. Which of the following people would be considered unemployed?
    A. Abe, who is retired.
    B. Lenny, who is working part time at a fast food restaurant.
    C. Homer, who lost his job at the power plant and is not looking for work.
    D. Edna, who lost her job as a teacher and is currently searching for a new job.

26. In a small country, the population equals 5,000. There are 4,000 people in the labour force and 3,000 people are employed. The unemployment rate equals _____.
    A. 0.6
    B. 0.75
    C. 0.25
    D. undetermined amount given the lack of information.

Refer to ***Exhibit 3*** for question no.27.

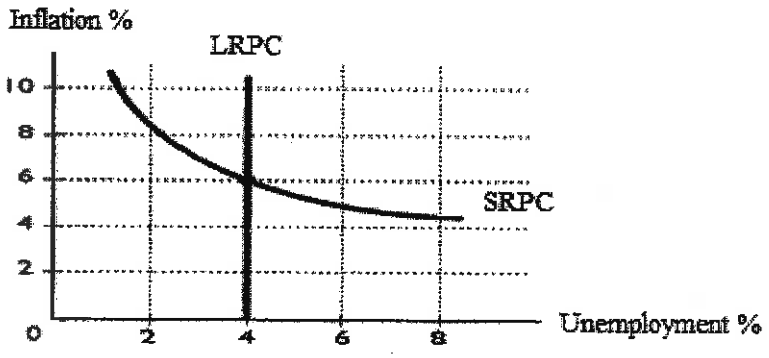

Exhibit 3

27. Based on ***Exhibit 3***, the natural unemployment rate is _____.
    A. 2 percent
    B. 4 percent
    C. 6 percent
    D. 8 percent

28. Tariffs and import quotas differ in that _____.
    A. one is legal, while the other is not
    B. one is a tax, while the other is a limit
    C. one is a form of trade restriction, while the other is not
    D. one is imposed by the government, while the other is imposed by the private sector

29. The consumption possibilities curve shows the combinations of goods that can be _____.
    A. produced by a nation after trade begins
    B. consumed by a nation before trade begins
    C. consumed by a nation after trading begins
    D. produced by a nation before trading begins

Continued...

30. When the principle of comparative advantage is used to guide trade, then a country will specialise by producing only _____.
    A. goods with the highest opportunity cost
    B. goods with the lowest opportunity costs
    C. goods for which production costs are more than average total costs
    D. goods for which production takes fewer worker-hour than another country

31. Which of the following correctly completes this statement? Gains from trade are _____.
    A. unrelated to the terms of trade
    B. the same as decreasing costs of production
    C. achieved when a country can consume beyond its production-possibilities frontier
    D. all of the above

32. Thailand has a comparative advantage in rice and an absolute advantage in cell phones. Indonesia has a comparative advantage in cell phones and an absolute advantage in rice. According to this scenario _____.
    A. Thailand should import both cell phones and rice
    B. Indonesia should export both cell phones and rice
    C. Thailand should export rice and import cell phones
    D. Indonesia should export rice and import cell phones

33. All of the following would be credit items in the U.S. balance of payments **EXCEPT** _____.
    A. capital inflows
    B. merchandise exports
    C. private gifts to foreigners
    D. payments for U.S. services to foreigners

34. Suppose you own some German government bonds that pay you interest every year. This interest is entered into which of the balance of payments accounts?
    A. trade account
    B. current account
    C. capital account
    D. official settlements account

35. When U.S. official reserves _____, the official settlements account balance becomes negative and when U.S. official reserves _____, the official settlements account balance becomes positive.
    A. increase; increase
    B. decrease; increase
    C. increase; decrease
    D. decrease; decrease

Continued...

36. If the current account balance has a $70 million deficit and there was no change in official reserves during that year, then we know that _____.
    A. the capital account balance must have a $70 million deficit
    B. the balance of payments must register a $70 million surplus
    C. the capital account balance must have a $70 million surplus
    D. the official settlements account balance must have a $70 million surplus

37. According to the theory of Purchasing Power Parity, if Japanese prices increase by 10 percent, while U.S. prices remain constant _____.
    A. the yen will depreciate
    B. the dollar will depreciate
    C. the demand for Japanese goods will rise
    D. Japanese goods are immediately less expensive in the U.S

38. Today, one U.S. dollar exchanges for 1.10 euros. The next morning the same dollar exchanges for 1.07 euros. We can conclude that the dollar has _____ and the euro has _____.
    A. appreciated; appreciated
    B. depreciated; appreciated
    C. appreciated; depreciated
    D. depreciated; depreciated

39. On the foreign exchange market, an increase in a country's exchange rate _____.
    A. decreases the demand for its currency and shifts the demand curve leftward
    B. decreases the demand for its currency and shifts the demand curve rightward
    C. decreases the quantity demanded of its currency and leads to a movement up along the demand curve
    D. increases the quantity demanded of its currency and leads to a movement up along the demand curve

40. If an English suit costs £200 and the dollar exchange rate is $1.50 per £, the suit would cost an American _____.
    A. $200
    B. $400
    C. $300
    D. $133.33

Continued...

SECTION B: STRUCTURED QUESTIONS [60 MARKS]

Instructions: Answer **ALL** questions in this section. Write your answers in the Answer Booklet.

Question 1

Part A

A bank has reserves of $50,000, deposits of $100,000 and loans of $50,000. Assume the required reserve ratio is 20 percent.

a) What are the bank's assets and what are its liabilities?

(1.5 marks)

b) How much does the bank have in excess reserves?

(2 marks)

c) Calculate the additional loans that can be made by the bank?

(1 mark)

d) What is the value of money multiplier?

(1.5 marks)

e) By how much will total deposits expand if this bank lends all its excess reserves and there is no leakage from the banking system?

(2 marks)

Part B

Exhibit 4 shows equilibrium in money market.

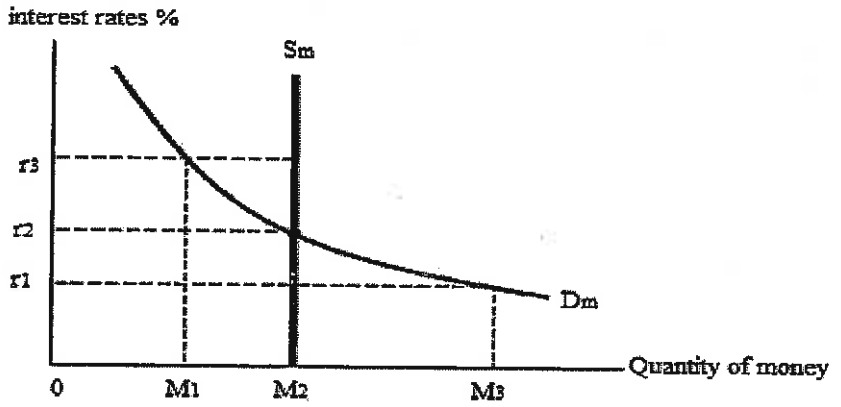

Exhibit 4

Based on ***Exhibit 4***, answer the following questions.

a) Which interest rate would result in an excess demand for money? What would eventually happen to the interest rate?

(1.5 marks)

b) Which interest rate would result in an excess supply for money? What would eventually happen to the interest rate?

(1.5 marks)

c) List the **TWO** factors that can cause money demand curve shifts rightward.

(1 mark)

Continued...

Part C

Suppose the population in Country Z is 180 million. Also assume that the working-age population is 150 million, the labour force is 125 million, and the employment is 120 million.

a) Calculate Country's Z labour force participation rates and the unemployment rates?

(4 marks)

b) Now suppose that 2 million students graduate from college in Country Z begin to look for jobs. What is the new unemployment rate if none of the students have found jobs yet?

(2 marks)

c) Suppose that all 2 million students find jobs. What is the unemployment rate now?

(2 marks)

[TOTAL 20 MARKS]

Question 2

Part A

Assume the following information for the United States and Mexico. The United States can produce a maximum of 600 bushels of barley or a maximum of 600 bushels of corn. Mexico can produce a maximum of 200 bushels of barley or 400 bushels of corn.

a) Suppose each country is self-sufficient and divides its resources equally between the two goods. What is the number of bushels of corn and barley does each country produce?

(2 marks)

b) What is the opportunity cost of a bushel of corn for each country?

(2 marks)

c) What is the opportunity cost of a bushel of barley for each country?

(2 marks)

d) Which country has a comparative advantage in producing corn? Briefly explain.

(1 mark)

e) Which country has a comparative advantage in producing barley? Briefly explain.

(1 mark)

f) If the two countries split the difference between the buyer's willingness to pay and the seller's willingness to accept, what are the terms of trade for corn?

(1 mark)

g) Suppose each country specialises in the good for which it has comparative advantage, and they exchange 200 bushels of corn for some bushels of barley. Compute the consumption bundles of corn and barley for each country.

(2 marks)

Continued...

Part B

Exhibit 5 shows the U.S. demand and supply curves of canned peaches.

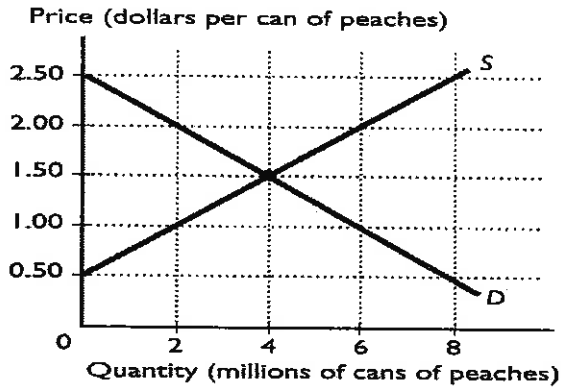

Exhibit 5

a) In the absence of trade, what would be the price of canned peaches and the level of production in the United States?

(2 marks)

b) If the world price of canned peaches is $2 a can and the United States engages in trade, what is the quantity produced in the United States and what is the quantity consumed? Does the United States import or export canned peaches? What is the quantity imported or exported?

(2 marks)

c) Calculate the value of consumer surplus before and after trade.

(2 marks)

d) Calculate the value of producer surplus received by sugar producers before and after trade.

(2 marks)

e) If trade is allowed, who gains and who losses, the consumers or the producers?

(1 mark)

[TOTAL 20 MARKS]

Continued...

Question 3

Part A

Exhibit 6 depicts the international transactions of Country A measured in millions of dollar.

Items	millions ($)
Merchandise exports	2,200
Export of services	300
Income from Country A assets abroad	900
Merchandise imports	3,000
Import of services	400
Income from foreign assets in Country A	500
Net unilateral transfers	-110
Outflow of capital	160
Inflow of foreign capital	600
Statistical discrepancy	180

Exhibit 6

Based on ***Exhibit 6***, calculate

a) merchandise trade balance. Did Country A run a trade deficit or trade surplus? Briefly explain.

(2.5 marks)

b) current account balance.

(3.5 marks)

c) capital account balance.

(2 marks)

d) official reserve balance.

(3 marks)

Part B

Exhibit 7 shows supply and demand schedules for dollar in the foreign exchange market.

RM per dollar	Quantity of dollar demanded (millions)	Quantity of dollar supplied (millions)
3.00	800	200
3.25	600	350
3.50	500	500
3.75	400	600
4.00	300	700

Exhibit 7

a) Determine the equilibrium exchange rate.

(1 mark)

Continued...

b) In the foreign exchange market, how will each of the following influences affect the demand for dollars and the demand curve for dollars?
   i. an increase in the U.S. interest rate.
   ii. a fall in the expected future value of dollar.

(4 marks)

c) Determine what would be the effect on the Malaysia balance of payments if the value of dollar is fixed at RM3.25 per dollar. Has ringgit overvalued or undervalued? If Malaysia wishes to maintain the fixed exchange rate, will the Malaysia's central bank need to buy dollar in exchange for ringgit or sell dollar in exchange for ringgit? What will happen to Malaysia's international reserves if the fixed exchange rate is maintained at RM3.25 per dollar?

(4 marks)

[TOTAL 20 MARKS]

End of Paper